



Date of Release: April 6, 2018

DBRS Confirms Ontario Power Generation Inc. at A (low)/R-1 (low), Stable Trends

Bloomberg: DBRS Confirms OPG at A (low), Stable

Industry Group: Corporate Finance

Sub-Industry: Utilities & Independent Power

Region: Canada

DBRS Limited (DBRS) confirmed the Issuer Rating and the Unsecured Debt rating of Ontario Power Generation Inc. (OPG or the Company) at A (low) and its Commercial Paper (CP) rating at R-1 (low). All trends are Stable. The ratings of OPG continue to be supported by (1) the reasonable regulatory regime in place for the Company's regulated generation facilities, (2) strong cash flow-to-debt and debt-to-capital ratios and (3) continuing financial support from its shareholder, the Province of Ontario (the Province; rated AA (low) with a Stable trend by DBRS). The Province, through its agent the Ontario Electricity Financial Corporation (rated AA (low) with a Stable trend by DBRS), provides most of OPG's financing (approximately 48% of consolidated debt). The Company's remaining debt includes project financing (33%), non-recourse debt issued by the Fair Hydro Trust (9%), CP (2%) and Senior Notes issued under the Medium Term Note Program (8%).

In March 2017, the Province announced its Fair Hydro Plan to reduce customer bills by 17% (plus an 8% HST rebate for a total reduction of 25%), with the Independent Electricity System Operator (IESO; rated A (high) with a Stable trend by DBRS) recording the monthly shortfall (as a result of the rate reduction) in a regulatory variance account. Under Bill 132, *Fair Hydro Act, 2017*, OPG was appointed as the Financial Services Manager for the creation of a financing entity (Fair Hydro Trust; Senior Notes rated AAA (sf) by DBRS) that may acquire an investment interest in the regulatory variance account from the IESO. DBRS does not expect the Fair Hydro Plan to negatively impact the Company's credit profile as (1) the Fair Hydro Trust is bankruptcy remote and ring-fenced from OPG (all debt is, and will be, non-recourse to the Company); (2) while OPG is expected to acquire up to 49% of the debt that will be issued by the Fair Hydro Trust, 44% will be funded through equity injections from the Province (with the remaining 5% to be funded by OPG); and (3) the Subordinated Notes and Junior Subordinated Notes to be acquired by the Company are rated AA (sf) and A (sf), respectively, by DBRS.

In December 2017, the Ontario Energy Board issued its decision on OPG's application for 2017–2021 rates. OPG had applied to transition to five-year incentive rate-setting (IR) regimes, with the hydroelectric facilities to operate under Price Cap IR and the nuclear facilities under Custom IR. This transition is not expected to materially affect the Company as (1) the hydroelectric segment has relatively stable generation output, (2) the nuclear production forecast takes into account the ongoing Darlington Refurbishment and (3) OPG can initiate a regulatory review if actual return on equity (ROE) falls 300 basis points below the approved ROE. However, DBRS believes the inclusion of stretch factors (0.3% for hydroelectric and 0.6% for nuclear) and the disallowance of \$100 million per year from the nuclear operations, maintenance and administration budget will likely result in continuing weakness in OPG's profitability. In 2017, excluding



a one-time gain on the sale of its head office, the Company recorded a corporate ROE of 5.1%, significantly below the allowed regulatory ROE of 8.78%. DBRS notes that this can be partly attributed to OPG's capitalization above the deemed equity component of 45%, and because new rates were approved to be effective June 1, 2017, instead of January 1, 2017, as applied. DBRS views a rating upgrade in the short-term to be unlikely because of the Company's current large capital expenditures program. A downgrade could occur should there be significant cost overruns with the Darlington Refurbishment that result in stranded costs.

Notes:

All figures are in Canadian dollars unless otherwise noted.

The principal methodologies are Rating Companies in the Regulated Electric, Natural Gas and Water Utilities Industry (September 2017), DBRS Criteria: Commercial Paper Liquidity Support for Non-Bank Issuers (April 2018) and DBRS Criteria: Guarantees and Other Forms of Support (January 2018), which can be found on dbrs.com under Methodologies.

The related regulatory disclosures pursuant to the National Instrument 25-101 *Designated Rating Organizations* are hereby incorporated by reference and can be found by clicking on the link under Related Documents or by contacting us at info@dbrs.com.

The rated entity or its related entities did participate in the rating process for this rating action. DBRS had access to the accounts and other relevant internal documents of the rated entity or its related entities in connection with this rating action.

For more information on this credit or on this industry, visit www.dbrs.com or contact us at info@dbrs.com.

Issuer	Debt Rated	Rating Action	Rating	Trend
Ontario Power Generation Inc.	Issuer Rating	Confirmed	A (low)	Stable
Ontario Power Generation Inc.	Unsecured Debt	Confirmed	A (low)	Stable
Ontario Power Generation Inc.	Commercial Paper	Confirmed	R-1 (low)	Stable



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